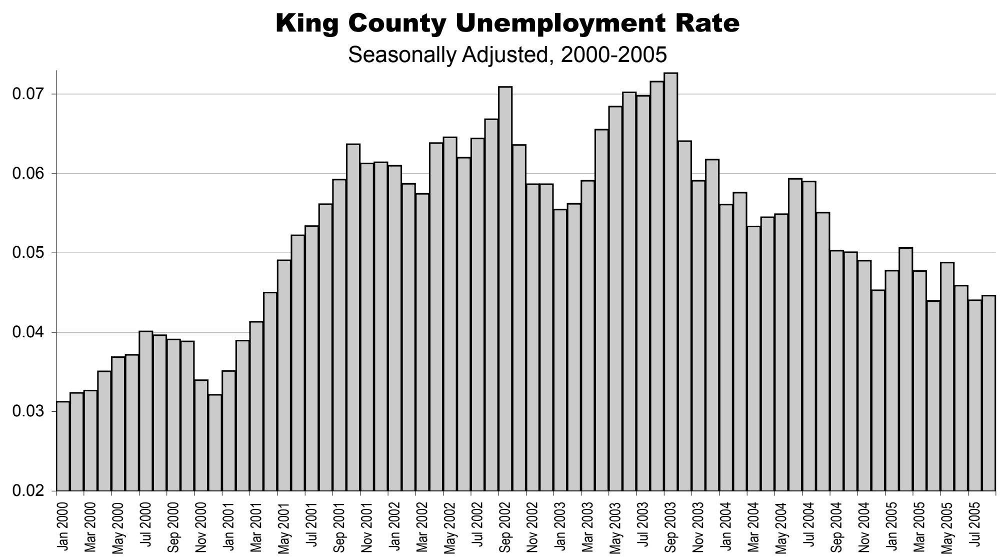
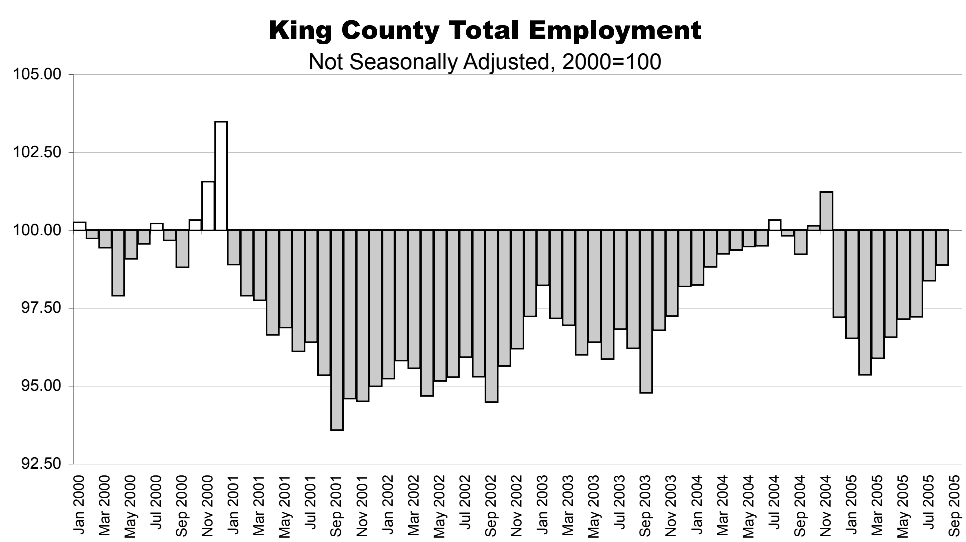
INTRODUCTION

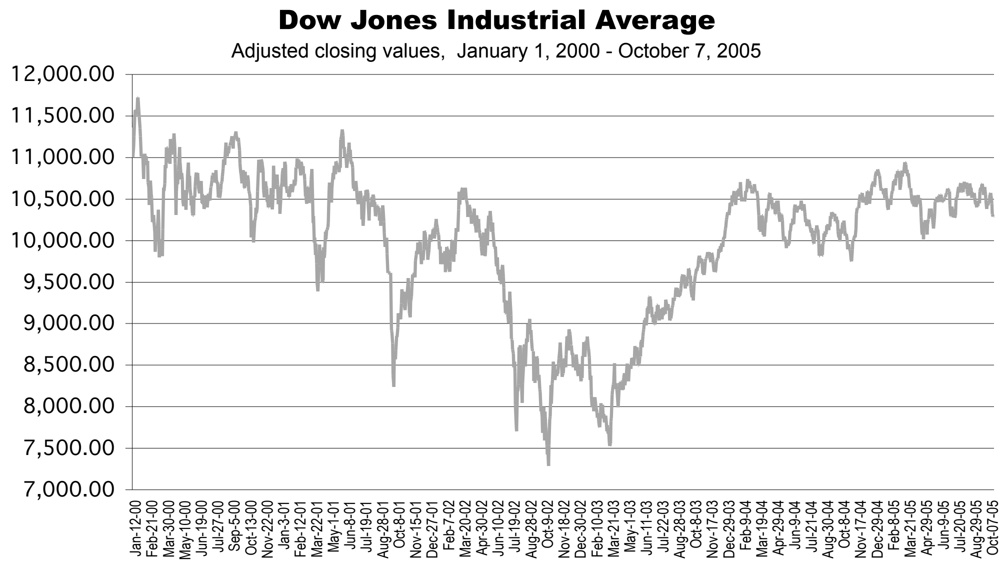
Robust growth has finally erased a four-year economic slowdown in King County. While income and employment changes remain short of the four years of rapid growth in the late 1990s, the marked improvement in local conditions reflects a return to equilibrium. Since mid-2000, the region has weathered a series of setbacks, punctuated by the dramatic collapse in equity market valuations, the September 11, 2001 terrorist attacks, myriad accounting scandals, and the buildup and continued aftermath of war in Afghanistan and Iraq. Halting recovery has now given way to unmistakable growth, but the improvement only belies the magnitude and duration of the 2001 recession.

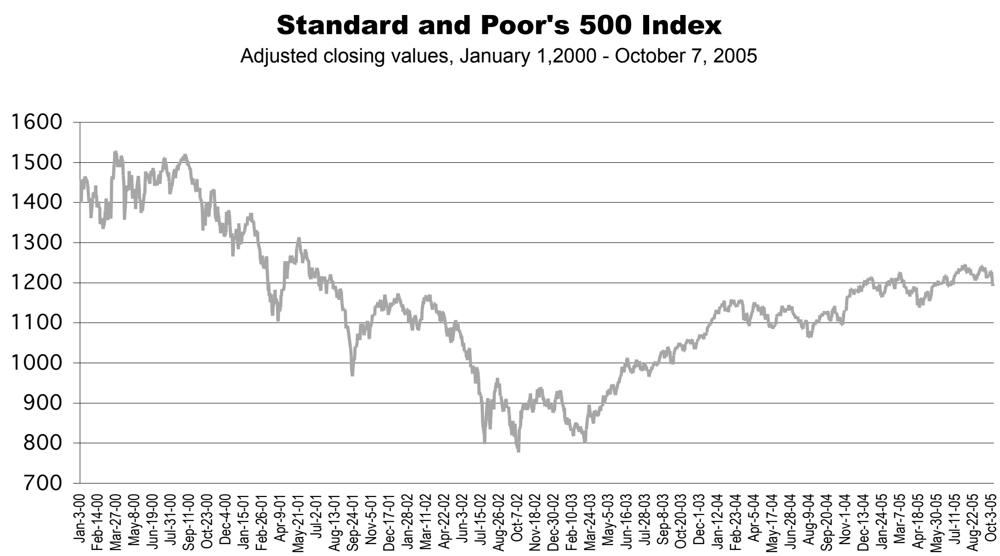
For the first time since the spring of 2001, the county is experiencing sustained seasonally adjusted unemployment of less than five percent. After three years of fitful growth, local business activity has surged in the last nine months, showing surprising strength in the absence of strong expansion in national markets. Having finally broken the cycle of improvement (such as in the second half of 2003) followed by stalled growth (as in the second quarter of 2004), the national economy is now increasingly threatened by heightened energy costs.

For 2006, the King County Office of Management and Budget anticipates sustained growth in the national economy. This forecast, developed by surveying local economists, published state and national forecasts, and county econometric models, is the basis for 2006 revenue and expenditure projections. Initial estimates of 2007 and 2008 revenues and expenditures are also prepared from this forecast for the out-year current expense subfund financial plan.









REVIEW OF ECONOMIC CONDITIONS

Statistically, the national recession may have ended in November 2001. The jobless recovery that followed lasted well into 2004, generally resulting in more dislocation than the actual recession.

Steady labor market improvement comes after setting a 22-year seasonally-adjusted high unemployment rate of 7.26 percent in September 2003.[1] Adjusted for education status, age composition, and other demographics, peak unemployment from the 2001 recession rivaled the early 1970s for highest joblessness since the great depression.

This fall, total employment in King County will surpass 1 million for the first time since 2000.[2] Accounting for natural workforce increases from population growth to new college graduates, labor participation statistics remain low given the overall business cycle. Outside of a few high demand sectors like

1 Washington Department of Labor and Industries, Labor Market and Economic Analysis and King County Office of Management and Budget seasonal adjustment model.

2 Second Quarter Economic Report, King County Office of Management and Budget.

construction, jobs are considerably more scarce than at almost any point since the mid-1990s. The apparent negative correlation between labor force shares and educational attainment could come to even eclipse the twenty-five year decline in absolute unemployment rates.[3]

Inflation-adjusted median household income was unchanged in 2004 from 2003 and remains 3.8 percent below peak 1999 levels.[4] Stagnation in household income coincides with sustained productivity increases – productivity per worker hour is up nearly 15 percent since 2000.[5] Wage trends, however, reflect slower nominal growth that has lagged inflation.

Contemporary research has almost canonically demonstrated that when labor supply exceeds demand, worker bargaining power is diminished.[6] The conundrum in recent data lies in the apparent coincident decline of both wages and unemployment. The recent decline in the rate of unemployment has been driven less by job growth than by the relative decline in the total labor force – the proportion of the population seeking or holding jobs. Since January 2004, when employment unambiguously emerged from the 2001 recession, total non-farm payrolls have expanded at 187,000 net new jobs per month. This number is reasonable in itself, if tepid compared to previous recoveries (36 percent lower than 1993-1994 recovery).

In August 2005, labor force participation rose to 66.2 percent, but it remains lower than the pre-recession peak of 67.1 percent in March 2001.[7] There is little prospect of returning to 2000-2001 levels in the near future – over the last year, the rate has improved on average by only two basis points per month. An adjusted unemployment rate that considered those that have abandoned their job searches would be nearly three points higher than current published statistics. Analysis by the Economic Policy Institute suggests that only net job creation of in excess of 300,000 per month is needed to address substantial labor slack masked by low participation rates.

In contrast to the labor market situation, the broader economy is exhibiting marked improvement. Uneven Gross Domestic Product growth can be more a consequence of accounting subtleties rather than larger

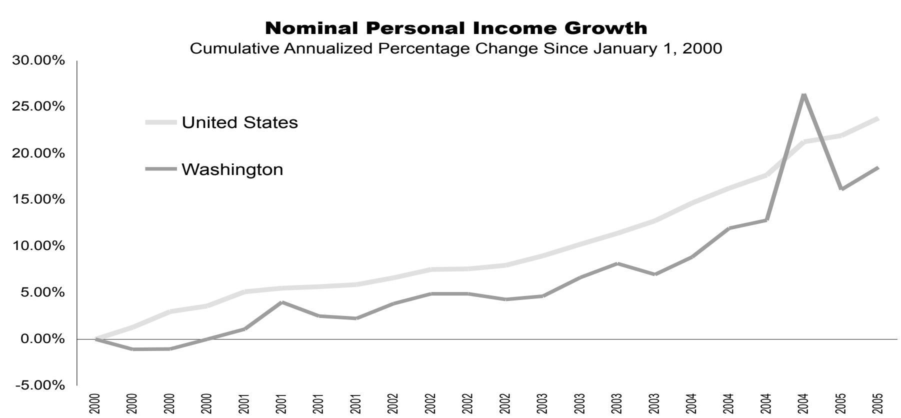
3 The Impact of Young Workers on the Aggregate Labor Market (2001) *Quarterly Journal of Economics*, 116: 969-1007.

4 US Department of Commerce, Bureau of the Census.

5 US Department of Labor, Bureau of Labor Statistics.

6 David G. Blanchflower & Andrew J. Oswald, 2005. "The Wage Curve Reloaded," NBER Working Papers 11338, National Bureau of Economic Research.

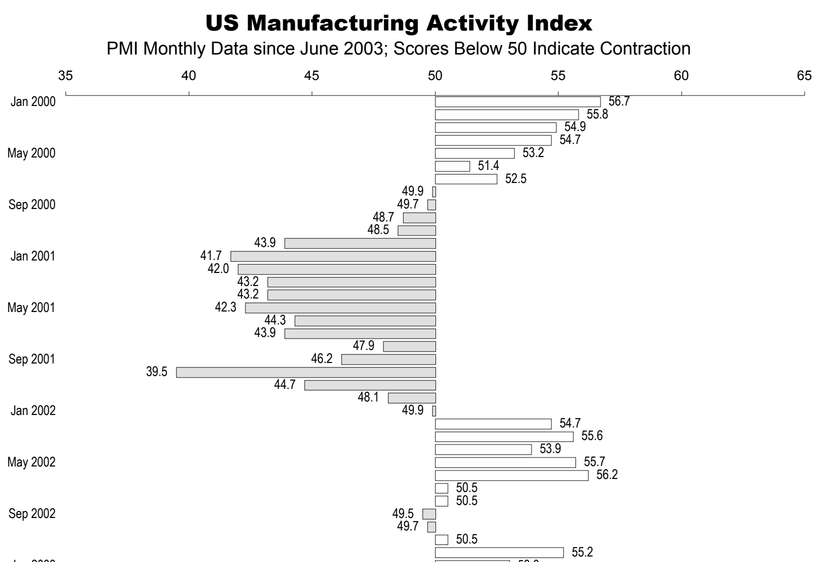
7 US Department of Labor, Bureau of Labor Statistics.

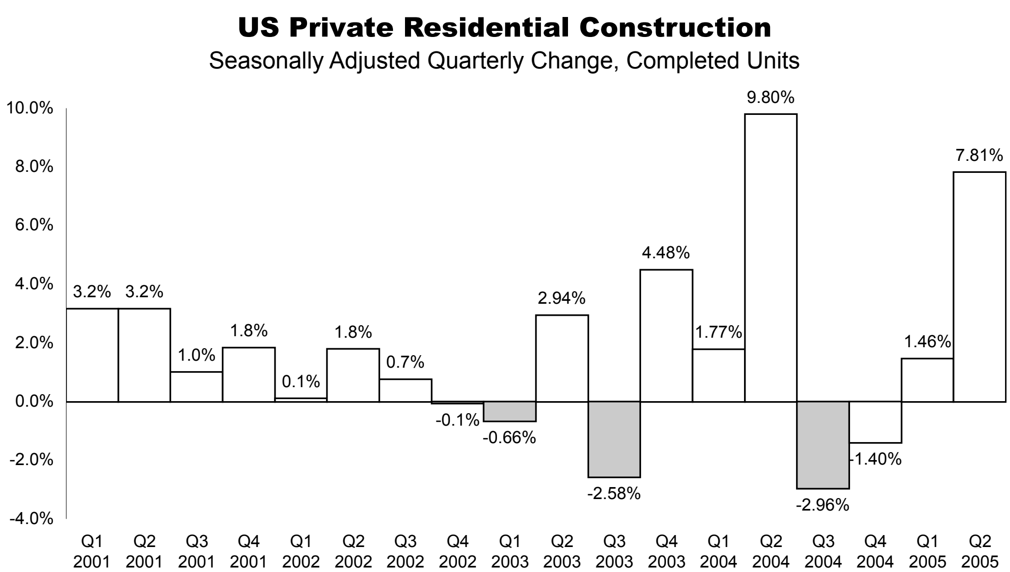


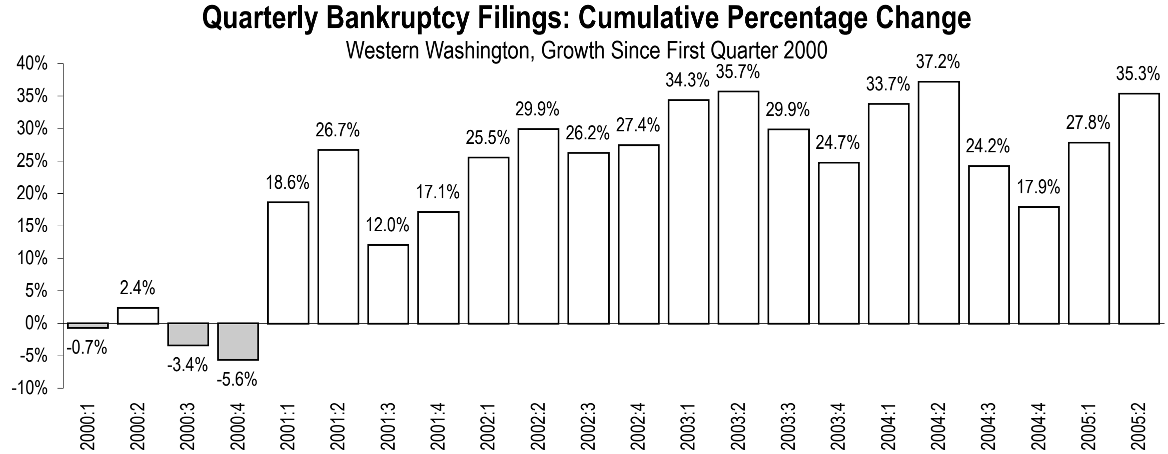
economic trends, but it has shown steadier movement in the last year.

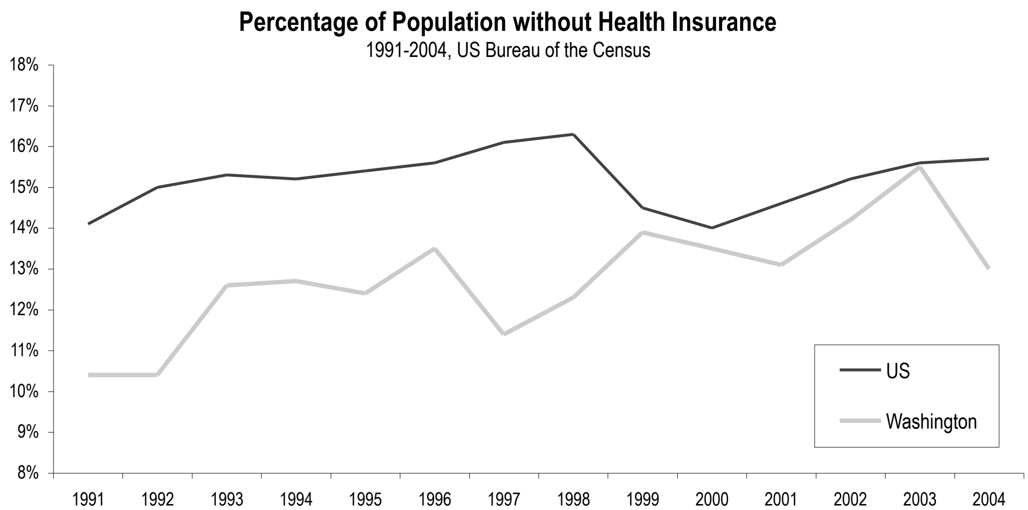
In late September, the Department of Commerce's second quarter estimate of GDP growth was 3.3 percent, identical to the second quarter of 2004, but lower than 2004 annual growth of 4.2 percent. A closer examination of second quarter data suggests a more optimistic interpretation. A decline in private inventories of $1.7 billion understates actual growth, while fixed investment surged from 5.7 percent growth in the first quarter to 8.8 percent in the second. After a barrage of increasingly poor trade balance news, these GDP numbers showed some improvement: exports were up 10.7 percent versus a decline in imports of 0.3 percent. Nonetheless, on an annual basis the trade deficit remains a staggering $691.0 billion, an improvement of just $6.5 billion from the first quarter – 5.58 percent of GDP.

The primary cause for concern has been consumer spending. Automobile and durable good purchases have shown weakness in recent months, and were unlikely to remain near peak levels anyway. Softening consumer demand has yet to affect the other linchpin of the recovery: housing. Residential construction and sales of both new and existing homes remain at or near record levels. Given the inevitable increase in long-term interest rates – and with them, mortgage rates – even the housing market will slow in the next year or two.









Perhaps the most immediate threat to the recovery lies in energy prices. Highly volatile commodity trading in light, sweet crude oil passed $70 per barrel for the first time in history in early September, driven by Hurricane Katrina and its aftermath. In the last 30 months, concerns about supply have rattled future markets, as production disturbances – both potential and realized – have emerged in succession in Iraq, Venezuela, Norway, Russia, Nigeria, and the hurricane ravaged US gulf coast. The fundamental problem, however, is one of demand, as oil consumption expands in developing countries, especially China. Excess production capacity has slipped precariously, and there is simply no margin to cover major supply disruptions.

The impact of high crude oil prices has driven even larger increases in retail gasoline in recent months. Part of this is the simple consequence of refinery disruptions from gulf coast storms, but it also appears to simply reflect the exercise of growing market power. Seasonal changes – winter heating oil production – typically result in higher gasoline prices under even the most tranquil market conditions. With refinery inventories unusually low, substantial energy price increases are possible this fall and winter, before receding in the spring.

Highly inelastic demand for oil requires substantial price increases to bring the market into equilibrium, which has in turn emboldened speculators. Sustained crude oil prices over $40 per barrel will increase inflation; prices in excess of $50 per barrel for any sustained period of time will undermine the short-term prospect for economic growth. The economy's ability to weather current prices in excess of $60 with little sign of broader inflation or diminished overall output is remarkable and unprecedented. In the long run, however, insufficient income growth and high consumer debt levels present a much larger danger to the economy than high energy prices.

Economic Assumption Summary

Percentage Change from Preceding Year

	2002	2003	2004	2005	2006	2007	2008
King County							
Employment	-0.6%	-0.7%	1.4%	2.7%	2.5%	2.0%	1.9%
Nominal Personal Income	1.5%	2.0%	4.4%	5.8%	6.0%	5.5%	5.4%
Housing Starts	32.9%	9.9%	5.8%	1.1%	-12.8%	-1.4%	0.6%
Population	1.0%	0.3%	0.5%	0.9%	1.0%	0.9%	0.9%
Consumer Price Index *	1.9%	1.6%	1.3%	3.3%	2.5%	2.6%	2.5%
COLA **	2.32%	2.00%	2.03%	2.19%	3.20%	2.00%	2.30%
Washington State							
Employment	1.7%	0.6%	1.7%	2.2%	1.9%	2.0%	1.9%
Nominal Personal Income	3.4%	3.5%	4.4%	5.3%	5.5%	5.2%	5.1%
Housing Starts	4.8%	6.5%	15.0%	1.2%	-7.9%	-1.1%	-0.1%
United States							
Employment	-1.1%	-0.3%	1.1%	2.0%	1.6%	1.6%	1.6%
Nominal Personal Income	2.7%	3.3%	5.6%	5.8%	5.5%	5.0%	5.1%
Housing Starts	6.5%	8.2%	2.7%	1.8%	-7.3%	-4.5%	-1.1%
Three-month Treasury Yield	-47.1%	-11.3%	34.0%	51.3%	18.8%	9.5%	7.5%
Consumer Price Index	1.6%	2.3%	2.7%	2.7%	2.4%	2.6%	2.5%
Real GDP	2.4%	2.7%	4.2%	3.7%	3.2%	3.0%	3.1%

* Puget Sound region

Locally, the impact of the September 11th terrorist attacks is fading. After dropping 6.4 percent between 2000 and 2002, total passenger traffic at Seattle-Tacoma International Airport has rebounded substantially. After the first eight months of 2005, traffic is running 2.8 percent above 2000 levels, on track to set a new record.[8] Hotel occupancy rates, buoyed by a resumption in convention activity and burgeoning cruise ship bookings, have dramatically strengthened. Vacancy rates near 40 percent in 2002 and 2003 have fallen to 29.6 percent over the first seven months of 2005, while discounting has abated and rates have stabilized.[9]

To be sure, problems remain. Despite low inflation, real per capita personal income is still below 2000 levels. In both 2001 and 2002, Real Per Capita Personal Income declined, for a cumulative change of negative 1.9 percent, offset only slightly by anemic growth since. Income levels are unlikely to exceed 2000 levels until 2006. More broadly, the most recent data indicate that Real Per Capita Gross State Product fell 1.6 percent in 2001.[10] Bankruptcy filings in Western Washington are up 35.3 percent since the start of 2000.[11]

Although the entire state has suffered during the downturn, the worst effects were focused on the Puget

8 Port of Seattle, *Airport Activity Report*.

9 Wolfgang Rood Hospitality Consulting.

10 US Department of Commerce, Bureau of Economic Analysis.

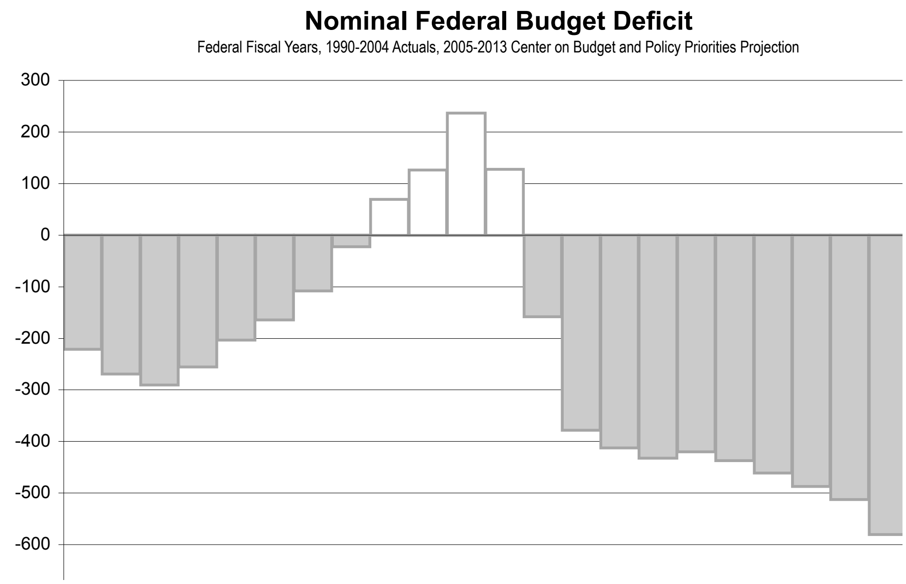
11 American Bankruptcy Institute.

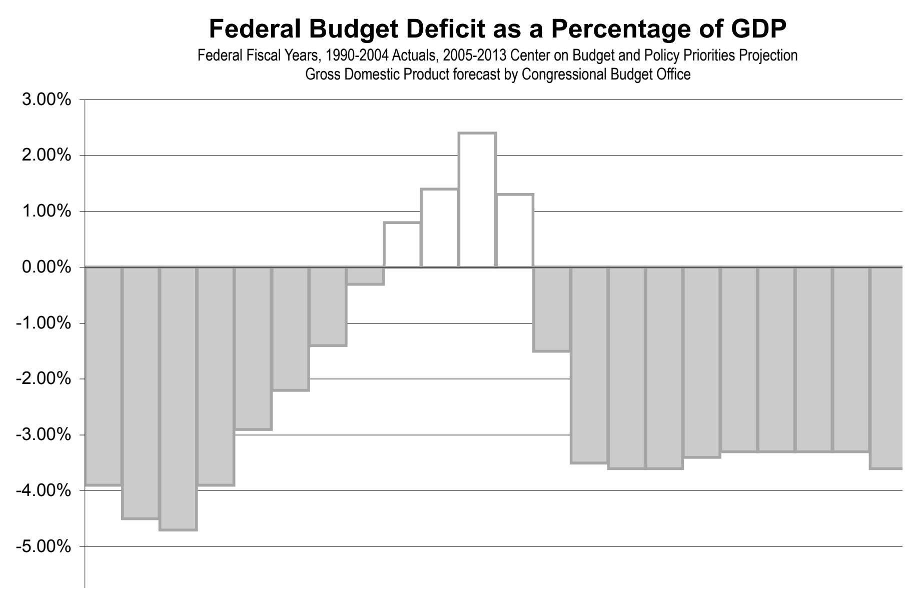
Sound region, and King County in particular. In the last twelve months, however, non-farm employment growth in King County has actually outpaced the rest of the state, 3.3 percent to 2.9 percent.[12]

The increase in employment has been unevenly distributed. After declining by 15.5 percent from 2002 to 2004, manufacturing employment is up 2.7 percent since July 2004. The 2002-2003 decline, occurred entirely in non-aerospace manufacturing, while the bulk of the 2004 decline was in aerospace and parts manufacturing. Growth in 2005 has been fueled by a turnaround in aerospace and parts, up 7.0 percent. By far the largest payroll growth has occurred in construction – up 7.9 percent since last July after growing 6.9 percent the year before. Other major sectors – health care, finance, insurance and real estate, and government employment – recorded between 1.5 and 1.9 percent growth.

Although health care employment has been strong, there are signs of problems ahead. Medical cost inflation, after abating in the mid-1990s, has returned to the growth rates of the late 1980s and early 1990s. Meanwhile the proportion of the population without health insurance has reached an all-time high in Washington State. The market for the direct purchase of insurance, which a decade ago covered 15 percent

12 Washington State Employment Security Department.





of Washington residents, now only serves 10.6 percent of the population.[13] Insurance is increasingly limited to employees of large companies and Medicare and Medicaid recipients.

Residential real estate continues to show remarkable strength. Sales in August are at near record levels, and prices have continued to appreciate in spite of economic conditions. The market has been strong, rapidly absorbing new housing stock from the residential construction boom. Residential construction has

13 US Bureau of the Census.

All King County Funds

Major Revenue Sources, 1998-2006

	1998 Adopted	1999 Adopted	2000 Adopted	2001 Adopted	2002 Adopted	2003 Adopted	2004 Adopted	2005 Adopted	2006 Proposed
TAXES	717,567,775	765,481,815	719,275,061	715,108,733	746,850,357	768,926,884	810,477,672	798,565,434	864,654,014
LICENSES & PERMITS	16,064,790	16,040,636	18,022,369	18,066,214	18,472,802	20,692,723	24,557,022	25,500,074	24,704,343
INTERGOVERNMENTAL REVENUE	28,640,718	26,756,947	26,756,947	26,756,947	35,829,205	-	-	-	-
FEDERAL GRANTS-DIRECT	24,137,304	26,852,073	28,650,976	30,207,497	32,359,967	36,380,703	36,012,144	36,048,518	32,813,722
FEDERAL SHARED REVENUES	721,204	732,617	678,590	688,182	699,091	1,069,761	1,080,642	1,094,152	1,322,569
FEDERAL GRANTS-INDIRECT	46,529,744	47,740,164	44,605,870	62,580,257	65,173,089	87,214,090	87,876,906	85,944,129	92,712,188
STATE GRANTS	81,134,564	81,737,617	99,941,683	103,615,392	100,044,636	122,000,403	131,252,575	50,890,604	50,605,285
STATE SHARED REVENUES	151,721	177,911	176,000	1,301,000	1,045,016	-	14,687	-	-
STATE ENTITLEMENTS	29,530,487	26,326,768	46,590,108	53,726,160	30,125,795	30,932,093	35,673,353	31,754,178	33,751,380
GRANTS FROM LOCAL UNITS	150,175	300,732	1,448,525	1,435,851	4,087,240	1,786,320	797,178	767,704	607,755
INTERGOVERNMENTAL PAYMENT	104,876,440	118,425,668	123,027,845	135,928,603	124,894,603	117,013,776	140,206,810	243,734,780	253,879,880
CHARGES FOR SERVICES	543,716,432	599,020,549	661,206,645	741,870,293	811,142,004	816,623,983	800,252,718	968,997,287	888,930,072
FINES & FORFEITS	6,300,462	6,493,323	7,069,093	7,232,871	7,537,213	7,803,918	9,119,402	8,290,176	7,317,592
STADIUM OPERATING REVENUES	9,744,434	6,853,074	221,000	-	-	-	150	-	-
OTHER	1,076,293,410	1,045,807,767	814,292,570	844,656,259	983,258,002	1,002,896,364	872,875,574	221,775,203	359,516,584
ALL FUNDS TOTAL	2,685,559,660	2,769,718,509	2,591,963,282	2,744,603,933	2,964,476,448	3,125,459,912	2,950,196,833	2,473,362,239	2,610,815,384

King County Current Expense Subfund

Major Revenue Sources, 1998-2006

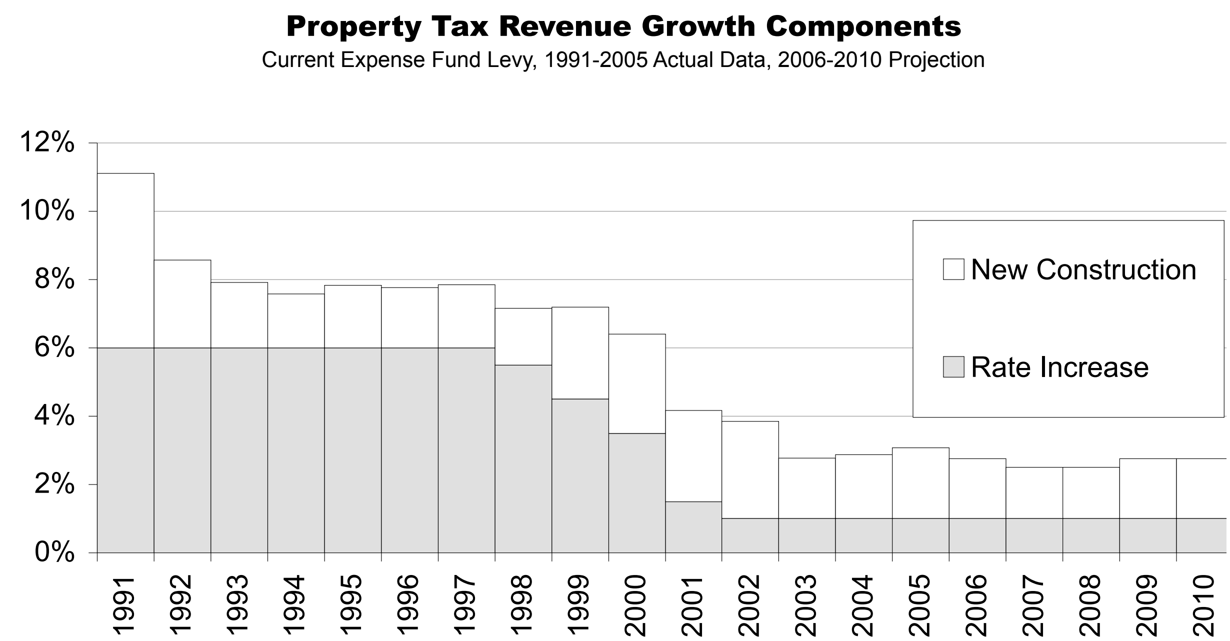
	1998 Adopted	1999 Adopted	2000 Adopted	2001 Adopted	2002 Adopted	2003 Adopted	2004 Adopted	2005 Adopted	2006 Proposed
TAXES	243,205,844	252,491,551	269,023,158	286,051,603	297,677,856	301,795,404	312,327,426	328,442,601	363,316,557
LICENSES & PERMITS	5,159,300	4,858,255	4,886,200	5,140,510	5,694,121	5,661,661	6,046,253	7,380,384	7,545,549
FEDERAL GRANTS-DIRECT	567,654	1,105,599	1,879,779	1,897,000	954,000	2,361,514	1,959,555	1,893,308	1,259,020
FEDERAL SHARED REVENUES	38,000	39,140	39,140	39,140	40,314	50,000	60,000	60,000	60,000
FEDERAL GRANTS-INDIRECT	4,293,999	4,657,898	4,328,755	5,900,152	4,817,776	6,546,708	6,734,208	7,951,779	8,168,949
STATE GRANTS	1,624,236	1,548,526	1,637,478	1,535,680	1,712,365	1,863,402	2,653,350	2,494,140	2,629,230
STATE SHARED REVENUES	141,000	167,030	176,000	176,000	181,280	-	-	-	-
STATE ENTITLEMENTS	1,317,000	1,257,917	1,297,505	1,554,125	1,383,967	1,424,505	1,407,505	6,559,055	6,993,579
GRANTS FROM LOCAL UNITS	70,728	20,320	14,000	14,000	2,614,420	-	-	-	-
INTERGOVERNMENTAL PAYMENT	46,388,515	49,080,342	52,656,427	55,772,028	56,733,723	52,269,056	56,001,858	53,164,198	55,623,169
CHARGES FOR SERVICES	57,621,784	70,993,265	76,991,057	80,258,079	82,639,182	89,547,761	84,746,544	89,803,336	96,966,895
FINES & FORFEITS	6,223,771	6,420,929	6,810,093	7,164,871	7,524,713	7,780,918	9,079,402	8,230,176	7,255,092
OTHER	33,800,723	24,250,729	25,658,174	25,082,650	19,903,635	18,503,578	23,280,217	23,294,922	33,534,781
CURRENT EXPENSE TOTAL	400,452,554	416,891,501	445,397,766	470,585,838	481,877,352	487,804,507	504,296,318	529,273,899	583,352,821

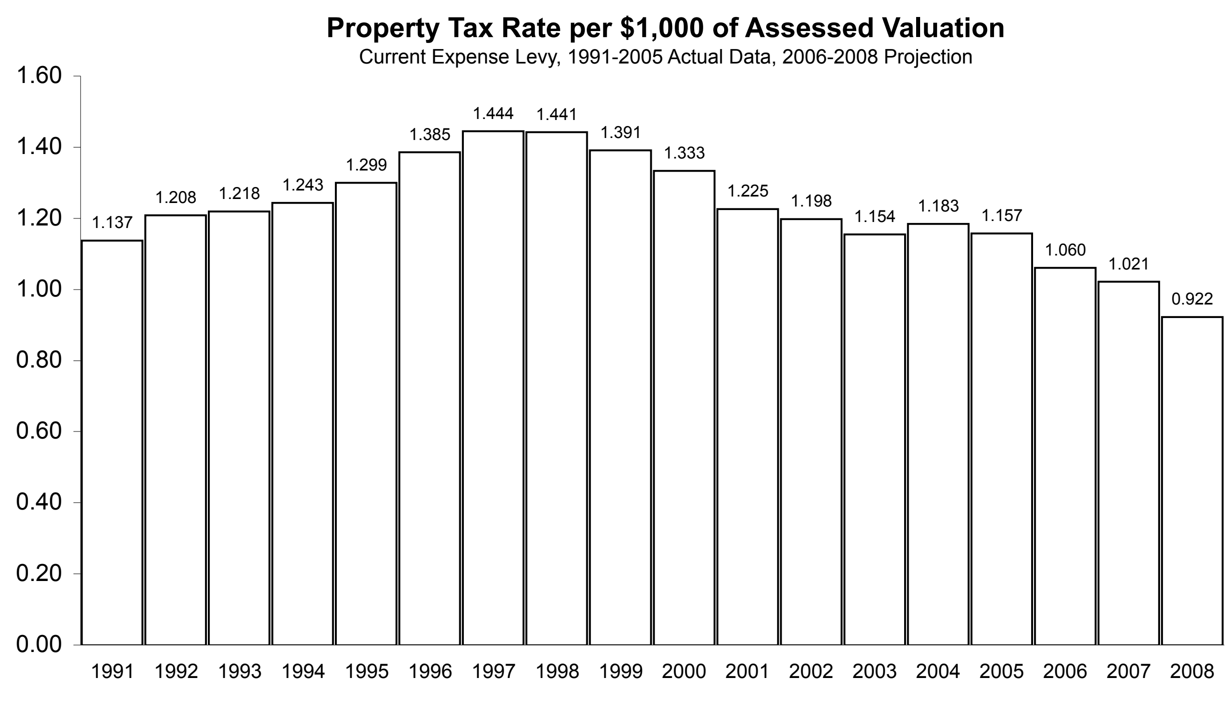
NOTE: Zero values for Intergovernmental and State Shared Revenues caused by phase-out of Title XIX and Motor Vehicle Excise Tax backfill funds, respectively.

been driven, in turn, by unprecedented low mortgage rates and, to a lesser extent, the complete collapse in commercial construction activity.

The local market for commercial real estate has stabilized. The commercial office space vacancy rate for Seattle continues to decline, down to 12.4 percent versus 14.2 percent and 16.2 percent in 2004 and 2003, respectively. Across the region, total vacant office space has also fallen, from 12.1 million square feet in 2003 to 9.9 million square feet in the second quarter of 2005.[14] In the coming year, the region will have to absorb two large vacancies – Washington Mutual's consolidation of over 2 million square feet of leased space in a new office tower adjacent to the Seattle Art Museum, and substantial redundancies anticipated at AT&T Wireless, recently acquired by Cingular Wireless. Aside from completion of a handful of long-standing projects predating the recession, no major increase in office space is expected from commercial construction over the next year.

14 Commercial Space Online, Inc. survey data [http://www.officespace.com] and Cushman and Wakefield.





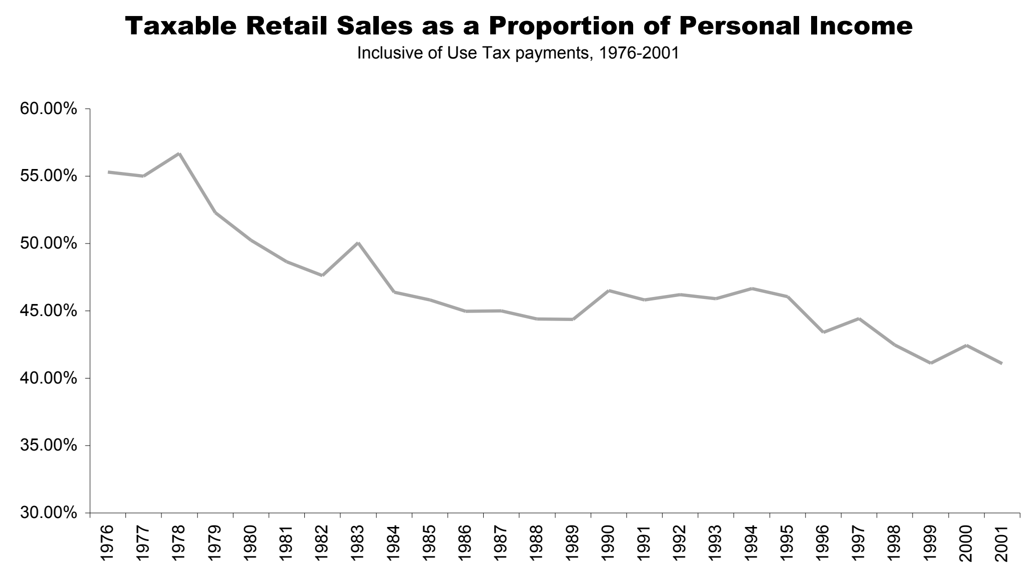
ECONOMIC FORECAST

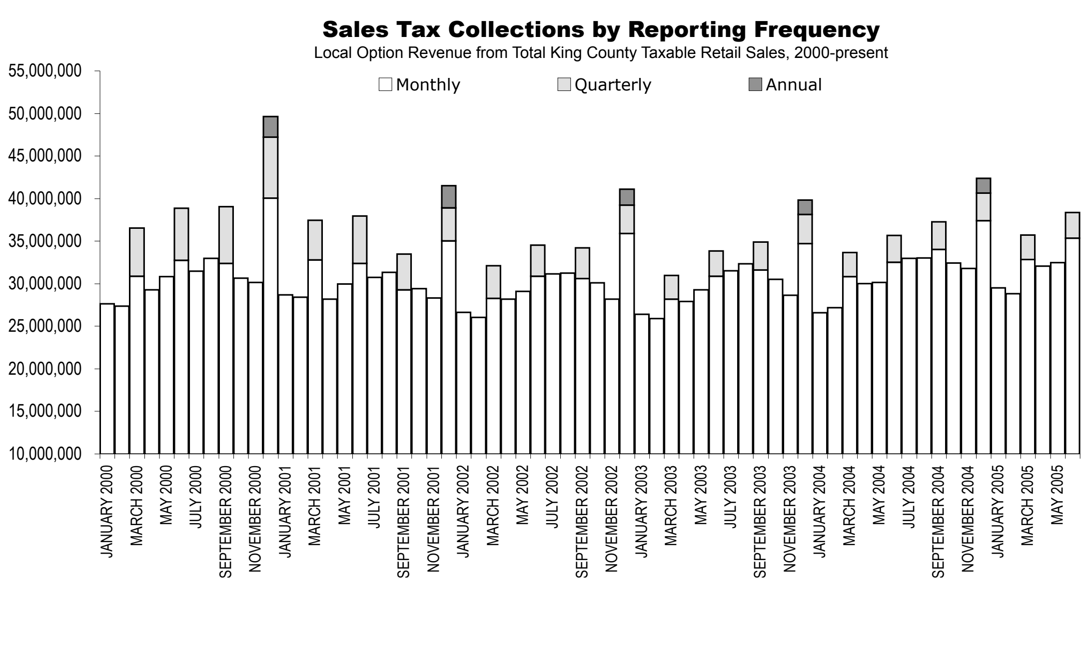
Entering 2004, Wall Street prognosticators feared that a booming economy would force a rapid increase in interest rates, undermining equity markets. The stock market has indeed stalled, but for the opposite reason. While the economy, at least as measured by Gross Domestic Product, has shown continued improvement, it has not been enough to make up for lingering labor market concerns, or energy price volatility.

Even as the Federal Reserve has acted to increase short-term interest rates, medium to long-term bond yields have actually fallen. Beyond soaring oil prices, or medical cost inflation, corporate balance sheets remain in excellent condition. Equity markets appear to be reflecting general concerns that the economy will slow, depressing earnings, rather than reacting to profitability prospects.

Clearly, continued hostilities in Iraq have also played a substantial role in unsettled financial markets. Given the almost certainty of a long-term US military deployment in Iraq for the foreseeable future, market conditions may not improve for some time.

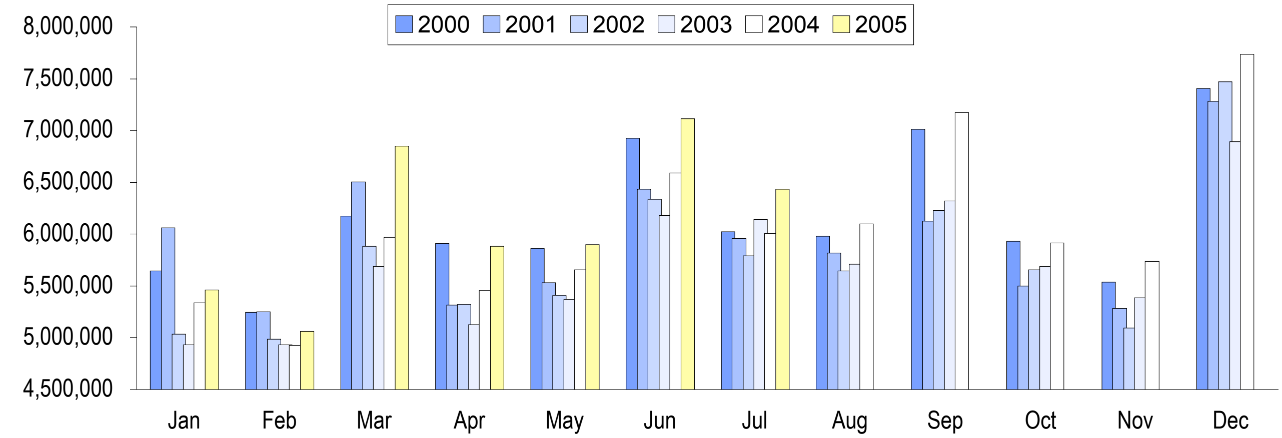
Over time, longer duration bond yields should rise and their prices fall as the Federal Reserve continues to tighten short-term rates. The inflationary pressure of higher energy prices will likely mandate Fed action, even if the economy falls well short of spectacular.





JULY FINAL October 08, 2005 10:19

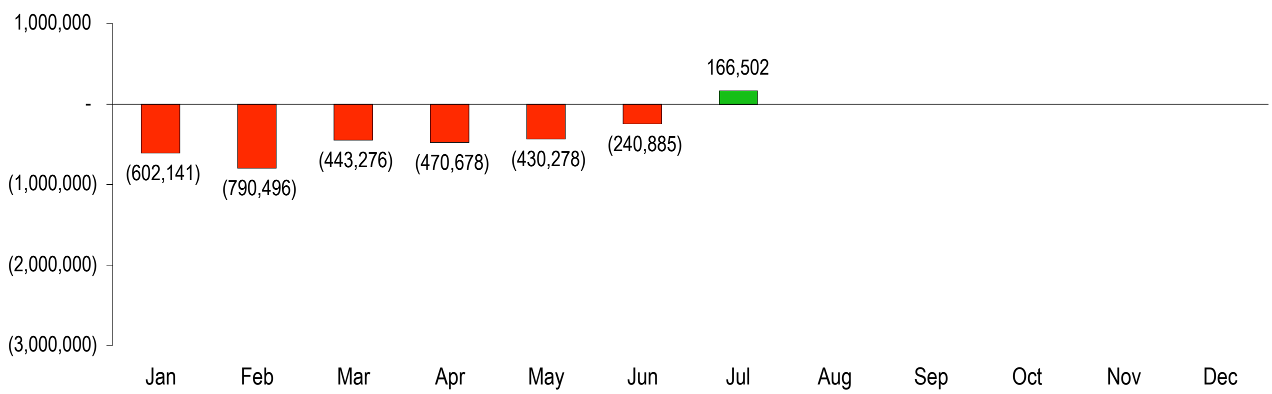
King County Monthly Sales Tax Collections



Monthly Collection Detail

	January	February	March	April	May	June	July	August	September	October	November	December
2000	5,643,746	5,247,801	6,175,848	5,908,357	5,860,285	6,924,611	6,023,919	5,982,095	7,013,757	5,929,100	5,534,585	7,407,359
2001	6,062,931	5,251,282	6,503,883	5,313,379	5,533,086	6,431,011	5,958,177	5,815,392	6,127,737	5,499,377	5,280,576	7,282,334
2002	5,036,669	4,988,719	5,884,638	5,321,370	5,407,187	6,339,046	5,792,913	5,645,463	6,228,228	5,656,303	5,096,438	7,471,553
2003	4,931,954	4,932,061	5,687,259	5,127,102	5,369,033	6,181,570	6,144,228	5,708,742	6,321,403	5,689,569	5,385,641	6,894,946
2004	5,338,022	4,928,659	5,970,150	5,454,094	5,657,854	6,592,828	6,004,537	6,096,735	7,175,660	5,912,824	5,737,184	7,738,012
2005	5,460,791	5,062,926	6,851,104	5,880,954	5,900,685	7,114,004	6,431,306					

Year-to-Date 2005 Variance from 2000-2001 Peak



Year-to-Date Collection Detail

	January	February	March	April	May	June	July	August	September	October	November	December
2000	5,643,746	10,891,548	17,067,396	22,975,752	28,836,037	35,760,649	41,784,567	47,766,662	54,780,419	60,709,520	66,244,105	73,651,464
2001	6,062,931	11,314,213	17,818,096	23,131,476	28,664,562	35,095,573	41,053,750	46,869,143	52,996,879	58,496,256	63,776,832	71,059,166
2002	5,036,669	10,025,388	15,910,026	21,231,396	26,638,583	32,977,629	38,770,542	44,416,005	50,644,233	56,300,536	61,396,974	68,868,527
2003	4,931,954	9,864,015	15,551,273	20,678,376	26,047,409	32,228,980	38,373,208	44,081,950	50,403,353	56,092,922	61,478,563	68,373,509
2004	5,338,022	10,266,682	16,236,832	21,690,926	27,348,780	33,941,609	39,946,146	46,042,880	53,218,540	59,131,364	64,868,548	72,606,560
2005	5,460,791	10,523,717	17,374,821	23,255,775	29,156,460	36,270,464	42,701,770					

* Data presented are total local option sales tax collections less Department of Revenue 1 percent administration fee. 90.4 percent of County sales tax receipts are deposited in the current expense fund. The remainder are dedicated to the Sales Tax Contingency Reserve (5.0 percent) and the Children and Families Set-Aside (4.6 percent).

Steady growth is anticipated in 2006, with business investment continuing to offset slackening consumer demand. Modest employment growth should accelerate, but a return to 1998-2000 levels is still two to three years away. Residential real estate and construction, carried three years by historically low long term interest rates, will return to more natural levels.

The Federal Reserve Board of Governors has increased the federal funds rate by 175 basis points so far this year, after 500 basis points of reductions starting in January 2001. The forecast anticipates 50 basis points in further increases over the rest of 2005 and early 2006. The Fed's stated preference for measured action suggests gradual and relatively predictable increases in short-term interest rates.

Strong regional employment growth should continue in 2006. Washington state recorded the highest increase nationally in personal income for both the second and fourth quarters of 2004, aided by the boost in payroll employment, strong 2003 equity market performance, and the start of Microsoft's unprecedented $75 billion special dividend and stock buyback. Notwithstanding this one time move from Microsoft, the extraordinary personal income growth attained in the late 1990s is unlikely to ever reoccur. The engine of technology boom personal income growth was the stock option; both market performance and structural changes suggest little further boost to income levels in the foreseeable future.

Compensation changes at Microsoft and across the industry have significantly reduced the variability – and positive upside – of employee stock ownership. Based on both market performance and the employee compensation policies, this forecast assumes only a limited boost to personal income levels from option and bonus income. Broader market valuations should continue to generally trend higher along the path of the second and third quarters of 2005, with little effect, positive or negative, on local conditions.

After rising by over 3.6 percent in both 2000 and 2001, growth in the Puget Sound region Consumer Price Index was just 1.9 percent and 1.7 percent in 2002 and 2003, respectively, driven by unchanged housing costs. In the first half of 2005, however, the CPI is up more than 2.4 percent. Obviously local prices remain dependent on global energy prices, as well as movement in agricultural goods, but core inflation – excluding energy and food – in the Puget Sound region should remain quite low for the next two to three years.

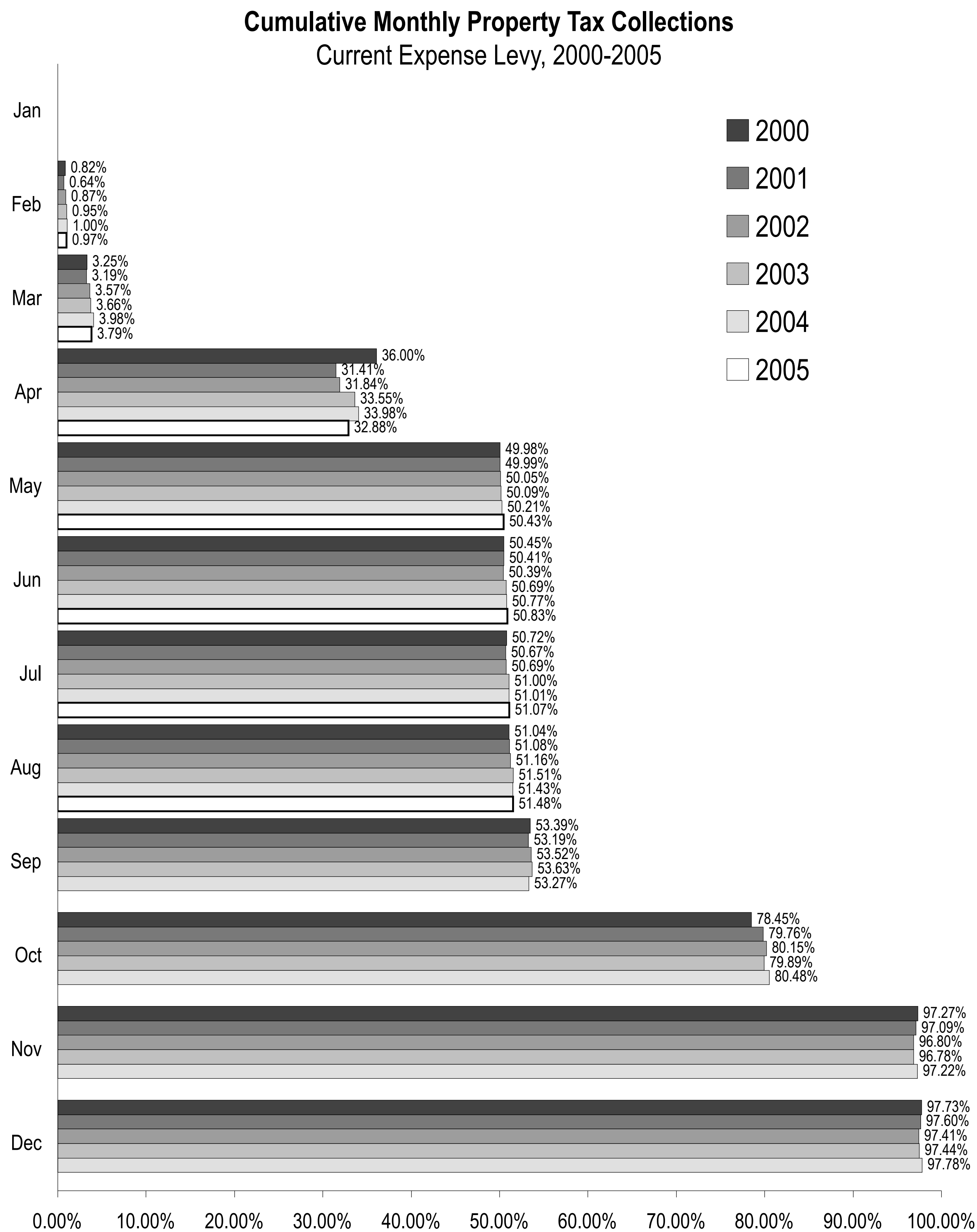
While not yet affecting the economic forecast, the startling rise in the federal budget deficit, and deteriorating outlook for the coming decade could undermine long-term interest rates.

KING COUNTY REVENUES

Total revenue into the county exceeds $2 billion dollars,[15] which King County distributes into over 50 separate funds. The largest funds include those for transit, wastewater, surface water management, roads, and the county general fund. The largest revenue source is taxes, followed by charges for services; together they account for over half of all revenues. Taxes include three major property tax levies, three different sales tax assessments, and taxes on real estate transactions. Charges for services include both direct contracts, interfund payments, and other services provided by the county.

Taxes are the largest source of revenues to King County, accounting for 33.1 percent of total revenues and 62.3 percent of current expense subfund revenue. The major tax sources for the county include property taxes, sales and use taxes, hotel and motel taxes, and telephone excise taxes to support the enhanced-911 system. Total King County tax revenue is projected to be $864.7 million in 2006, an increase of 8.3 percent from the adopted 2005 budget. These revenues support operating expenses, debt service, and some capital projects. Property taxes are the largest single tax source for the county, with a proposed levy of approximately $447.0 million in 2006, including $57.4 million collected for Emergency Medical Services, $20.4 million of which is disbursed directly to the city of Seattle.

15 Interfund transfers, overhead rates, and other transactions duplicate some funds in the total revenue figure of $3.2 billion.


Cumulative Monthly Property Tax Collections
Current Expense Levy, 2000-2005
2000
2001
2002
2003
2004
2005
Jan
Feb
0.82%
0.64%
0.87%
0.95%
1.00%
0.97%
Mar
3.25%
3.19%
3.57%
3.66%
3.98%
3.79%
Apr
36.00%
31.41%
31.84%
33.55%
33.98%
32.88%
May
49.98%
49.99%
50.05%
50.09%
50.21%
50.43%
Jun
50.45%
50.41%
50.39%
50.69%
50.77%
50.83%
Jul
50.72%
50.67%
50.69%
51.00%
51.01%
51.07%
Aug
51.04%
51.08%
51.16%
51.51%
51.43%
51.48%
Sep
53.39%
53.19%
53.52%
53.63%
53.27%
Oct
78.45%
79.76%
80.15%
79.89%
80.48%
Nov
97.27%
97.09%
96.80%
96.78%
97.22%
Dec
97.73%
97.60%
97.41%
97.44%
97.78%
0.00%
10.00%
20.00%
30.00%
40.00%
50.00%
60.00%
70.00%
80.00%
90.00%
100.00%

Sales Tax Forecast Detail

	2001 Actuals	2002 Actuals	2003 Actuals	2004 Adopted	2005 Adopted	2006 Pr
General Local Option						
Current Expense	64,237,486	62,258,958	61,154,089	62,062,318	65,871,140	71,79
Children and Family	3,268,722	3,168,044	3,111,823	3,158,038	3,351,850	3,65
Sales Tax Reserve	3,552,958	3,443,526	3,382,416	3,432,650	3,643,315	3,97
Total	71,059,166	68,870,529	67,648,329	68,653,007	72,866,305	79,42
Criminal Justice						
Total	10,958,675	10,485,286	10,331,066	11,074,145	11,295,913	11,96
Public Transportation						
Total	277,796,000	297,136,000	302,199,000	308,041,000	325,968,986	349,27

PROPERTY TAX

Property taxes are collected through the countywide levy, the unincorporated area levy, the Emergency Medical Services levy, and voter approved debt. These receipts are dedicated to various funds within King County.

Property taxes are limited by both county policy and state law. Under Initiative 747, approved by Washington voters in 2001 (but rejected by a majority of King County voters), the regular levy can grow at only one percent annually, plus the increase in new construction. With inflation typically running two or three percent, this measure is gradually decreasing the effective tax paid by typical property owners, and reducing the dollars available for the current expense fund.

The overall countywide levy is projected to decline from $286.6 million to $283.1 million in 2006.[16] The $12.2 million Automated Fingerprint Identification System (AFIS) levy expires at the end of 2005, and will be placed before voters for renewal in September 2006. No AFIS levy will be collected in 2006 since operational efficiencies will cover 2006 costs with remaining 2001-2005 levy proceeds.

The amount remaining for the current expense subfund is the total levy capacity less distributions for debt service, parks, river improvement, veterans, and other designations. Current expense revenues from the property tax levy are estimated at $234.8 million. New construction of 2.25 percent accounts for the increase.

The unincorporated area levy (traditionally known as the road levy) is proposed at $70.3 million for 2005.

16 The countywide levy includes the current expense fund and dedicated millage for mental health/developmental disabilities, river improvement, human services, veterans' aid, intercounty, limited bond redemption, and voter approved lid-lifts.

SALES TAX

Sales taxes constitute Washington's largest revenue source, and King County's second largest source of tax receipts. A sales tax rate of 8.80 percent is assessed in the county, distributed as follows:

6.50 percent is collected by the state;

1.00 percent is a local option tax divided between cities and the county;[17]

0.80 percent is collected to support Metro Transit;[18]

0.40 percent is collected by the Regional Transit Authority (Sound Transit);[19]

0.10 percent is collected to support criminal justice programs.[20]

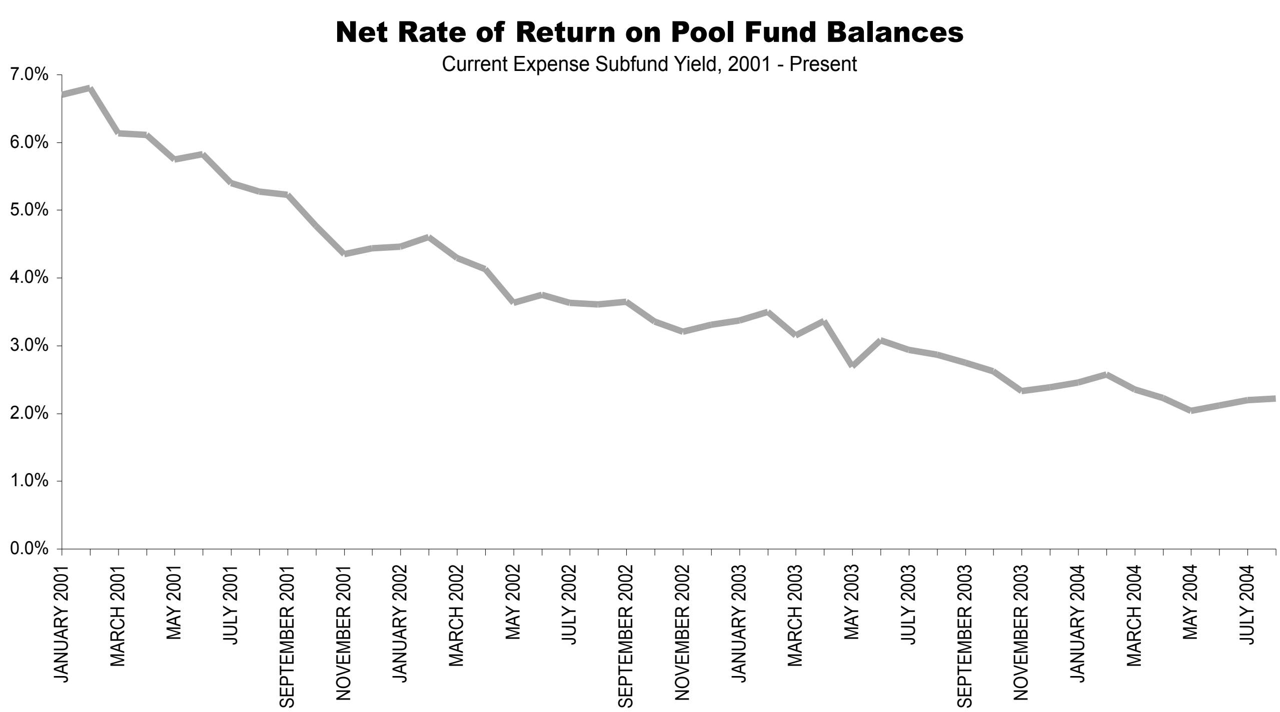
The sales tax is strongly influenced by changes in the economy and by the geographic areas from which it is collected. The public transportation and criminal justice funds receive revenues from countywide retail sales, with unincorporated areas constituting a little over four percent of the tax base. In contrast, over 17.6

17 Within cities, 0.15 percent is distributed to the county, and 0.85 percent to the city. King County receives the full 1.00 percent collected in unincorporated areas.

18 This tax was approved in April 2001 to replaced funds lost with the repeal of the Motor Vehicle Excise Tax by Initiative 695 in November 1999.

19 This tax is not collected in the rural part of King County where the sales tax rate is 8.40 percent.

20 90 percent of these funds are allocated to the cities on the basis of population. King County receives a share based on unincorporated population, in addition to the remaining 10 percent. This tax was approved by county voters in 1992.



percent of King County's general fund sales tax revenue is collected in unincorporated areas. Differences in the geographical composition of taxable retail sales also complicate analysis of revenue over the course of the business cycle. For example, the relative dominance of the construction sector in unincorporated King County makes the current expense subfund more sensitive to economic conditions than countywide taxes for transit and criminal justice.

Sales taxes place a disproportionate burden on lower income households. Over time, the inability to tax internet transactions and a general lag behind personal income growth will also prevent King County sales tax receipts from keeping pace with the cost of delivering most government services.

Purchases by King County residents from firms that do not operate in Washington are typically not subject to sales taxes. The rapid expansion of internet driven electronic commerce and Washington's high sales tax rates have provided a substantial incentive for consumer purchases over the internet to realize significant tax savings. A study published last July by researchers at the University of Tennessee has attempted to quantify the impact of internet and catalog sales on state and local sales taxes. The study concluded that roughly half a billion in state and local sales tax revenue was lost in Washington in 2003 due to remote purchases, forecasted to increase to $1.1 billion in 2008. These projections have been built into the outyear sales tax forecast.

Total projected 2006 general fund sales tax revenue is $91.4 million, an increase of 3.8 percent over estimated 2005 receipts. Of the total, $3.7 million will be deposited in the children and family services subfund while $4.0 million is earmarked for the sales tax reserve subfund, the proceeds of which are used to support major maintenance expenses. The remaining $71.8 million is dedicated to the current expense subfund. These subfunds, along with the inmate welfare subfund, comprise King County's general fund.

Real Estate Excise Tax

King County levies the Real Estate Excise Tax (REET) in unincorporated King County and administers state and city REET taxes throughout the county. Reflecting unprecedented low interest rates, real estate sales have been remarkably high in recent years. Tax collections have also been boosted in the last two years by three unusually large timber tract transactions. Reflecting the slowdown in construction and the decreased stimulus effect of low mortgage rates, high REET revenues will almost certainly decline in the coming year. REET consists of two 0.25 percent taxes on real estate transactions. Each is forecasted at just over $6.7 million in 2006.

Interest Earnings

Because of high volatility, attributable to variance in both interest rates and county fund balances, the Office of Management and Budget continues to provide a conservative interest earnings forecast. Interest rates have been projected using futures prices on the New York and London markets and correlating them with historic pool earning performance. For 2006, a rate of return of 4.100 percent is assumed. This forecast will be revised following the Federal Reserve Open Market Committee meeting on November 1, 2005.